



**US Army Corps
of Engineers**

Case Study #4

**Alternative Dispute
Resolution Series**



BECHTEL NATIONAL, INC.

August 1989

IWR Case Study 89-ADR-CS-4

The Corps Commitment to Alternative Dispute Resolution (ADR):

This case study is one in a series of case studies describing applications of Alternative Dispute Resolution (ADR). The case study is part of a Corps program to encourage its managers to develop and utilize new ways of resolving disputes. ADR techniques may be used to prevent disputes, resolve them at earlier stages, or settle them prior to formal litigation. ADR is a new field, and additional techniques are being developed all the time. These case studies are a means of providing Corps managers with examples of how other managers have employed ADR techniques. The information in this case study is designed to stimulate innovation by Corps managers in the use of ADR techniques.

These case studies are produced under the proponenty of the U.S. Army Corps of Engineers, Office of Chief Counsel, Lester Edelman, Chief Counsel; and the guidance of the U.S. Army Corps of Engineers Institute for Water Resources, Fort Belvoir, VA, Dr. Jerome Delli Priscoli, Program Manager.

For further information on the ADR Program and case study contact Program Manager:

*Dr. Jerome Delli Priscoli
Institute for Water Resources
Casey Building
7701 Telegraph Road
Ft. Belvoir, VA 22060-5586
Telephone: (703) 355-2372
Fax: (703) 355-3171*

Bechtel National, Inc.

Alternative Dispute Resolution Series

Case Study #4

Lawrence E. Suskind
Principal Investigator

Susan L. Podziba
and
Eileen Babbitt
Co-Investigators

Endispute, Inc.
955 Massachusetts Avenue
Cambridge, MA 02139

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CASE STUDY #4 BECHTEL NATIONAL, INC.

THE PROJECT AND CLAIM

SUMMARY

On April 6-10, 1988, Bechtel National Inc. (Bechtel) and the U. S. Army Corps of Engineers (Corps), Omaha District, used a mini-trial to settle a complex series of claims for \$3.7 million. The case consisted of seven separate claims, including those of major subcontractors, totalling, at the time of the mini-trial, \$21.2 million including interest*. Originally filed in the fall of 1986, the claims arose from modifications and impacts due to incomplete design plans for construction of the Consolidated Space Operations Center (CSOC) in Colorado.

Professor Ralph Nash served as the neutral, and Colonel Steven West, Omaha District Engineer, and E. Robert Jackson, Vice President at Bechtel Civil, Inc. were the decision-makers for the Corp and Bechtel. Gary Henningsen, Omaha District Counsel, presented the Corps case, and Jon Anderson, of Thelen, Marrin, Johnson & Bridges, served as counsel for Bechtel.

The main points illustrated by this case are: 1) the advantages and disadvantages of subcontractor participation in mini-trials; 2) strategies for managing complex technical information in settlement negotiations; 3) strategies for using working groups to develop components of a settlement agreement; 4) advantages and disadvantages of using decision-makers who are outside the emotional entanglement of the dispute; and 5) opportunities to use neutrals to provide various services.

BACKGROUND

In February 1984, the U.S. Army Corps of Engineers, Omaha District, contracted with Bechtel National, Inc. to build the Consolidated Space Operations Center in Colorado Springs, Colorado. The \$64 million lump sum contract specified a compressed construction schedule of 540 days to allow for building occupancy by August 1, 1985.

From the start, the project was plagued by problems associated with seemingly incomplete design plans, numerous requests for additional information from subcontractors, and ambitious completion dates. The government issued a number of acceleration orders early in the construction process. Negotiations between the Corps and Bechtel failed to resolve differences over price increases and the costs of indirect impacts, e.g. costs associated with the acceleration and modification orders. Bechtel subsequently filed a number of claims including several on behalf of its subcontractors, e.g. U.S. Engineering/Cobb Plumbing and Heating, Inc. and Marathon Steel, Inc.

By April 1987, Bechtel had received a final contracting officer's decision (COD) on only one claim, the "shielding claim," valued at \$750,000. In an attempt to force decisions on the others, Bechtel filed appeals at the Board of Contract Appeals on a "deemed denial"

* This is the figure quoted by Corps staff in a July 18, 1989 phone call.

basis.¹ In response, the Corps filed motions to dismiss the appeals on the grounds that the contracting officer lacked sufficient time to render decisions. (The Corps had hired a private consultant to determine the validity of the claims. The consultant had not yet completed his investigation at the time of the appeal.)

By October 1987, neither side had succeeded in even getting on the Board docket. At that time, Col. Steven West, the Omaha District Engineer, approached Bechtel with a suggestion that they use a mini-trial to settle all outstanding claims. West spoke directly with Robert Jackson and explained the ADR procedure. Following their conversation, West, Jackson, and their attorneys held a pre-ADR meeting at the Denver Stapleton Airport. As a result of the meeting, each side was assured the other would engage in a good faith effort to settle all claims. The attorneys then formalized the discussions and produced an ADR agreement.

CHRONOLOGY OF THE CLAIM

Bechtel was awarded the CSOC contract on February 9, 1984. The contract specified a compressed construction schedule in order to make the CSOC available by August 1, 1985. Construction commenced on February 25, 1984. In the fall of 1986, Bechtel submitted \$14 million in claims, including over \$6.5 million worth of subcontractor claims, for further compensation that stemmed from work changes required by the Government's unilateral modification orders, some of which were issued because negotiations failed to yield agreements on necessary works. Over time, Bechtel filed further claims, raising their total worth to \$21.2 million.

In February 1987, the Corps informed Bechtel of its plans to hire a private consultant to determine the validity of the claims. The expected report completion date was December 1987. Dissatisfied with this timetable, and after receiving a COD for only one claim by April 1987, Bechtel appealed all the claims on a "deemed denial" basis. As noted above, the government moved to dismiss the appeals on the grounds of insufficient time to render a contracting officers' decision. Bechtel responded with a motion for summary judgment² based on the fact that the government had conceded entitlement when it issued the multi-million dollar acceleration modifications.

By October 1987, no Board hearing dates had been set. Colonel Steven West raised the option of using a mini-trial to settle the claims and arranged a meeting of the potential mini-trial decision-makers and their attorneys. The meeting took place in December at the Stapleton Airport in Denver, after which the attorneys negotiated the details of the mini-trial agreement. It was signed on January 14, 1988. Bechtel and the subcontractors submitted quantum analyses on March 8, 1988, and the mini-trial was held in Omaha, Nebraska on April 6-10, 1988. The decision-makers reached a negotiated settlement on the evening of April 10th.

¹ The contractor assumed the contracting officer denied the claim since he failed to render a decision within a certain period of time.

² A summary judgment is a potentially despositive motion because it asks the court to grant a final decision based on the law and uncontested fact.

MAJOR ISSUES IN DISPUTE

The central issues in dispute concerned the direct and indirect impacts of government changes in work schedules and design. Bechtel claimed that government modification and acceleration orders had an adverse impact on its work schedule and led to uncompensated costs for additional materials and labor. Many of the work change orders were issued unilaterally-- that is, without any prior consultation with Bechtel, on the condition that prices would later be adjusted. However, Bechtel and the Corps failed to successfully negotiate such adjustments and the dispute developed into several claims.

The claims can be divided into three groups: those initiated by 1) Bechtel, 2) U.S. Engineering/Cobb Plumbing and Heating Company (U.S./Cobb) and several other subcontractors, and 3) Marathon Steel Company (Marathon). The Bechtel claims ask for cost adjustments based on additional indirect and direct costs associated with major design changes requested by the Government after Bechtel was awarded the contract. Many of these changes were based on assertions of deficiencies in the original design plans. The U.S./Cobb claims focused on the pricing of a number of work change orders and disagreements over the validity of additional material and its costs. The Marathon claims were based on assertion of the costs of construction changes ordered by the government and associated losses in productivity. (Marathon was paid \$2 million for the contracted work and claims it lost \$3.5 million.)

POSITIONS OF EACH SIDE PRIOR TO ADR

Prior to the mini-trial, the Corps and Bechtel did not engage in serious negotiations. The Corps had been waiting for a report from the Alpha Corporation (Alpha), an outside claims consulting firm hired to determine the validity of Bechtel's claims. By the time the Stapleton airport meeting took place, the Corps had determined partial entitlement in one major claim, but was still waiting for the full Alpha report. U.S./Cobb's rejection of a settlement offer coupled with possible personality clashes between negotiation personnel on the site, resulted in a disputed change order. This type of impasse often becomes a claim as a result of the Corps' issuance of a unilateral change order in accordance with the Corp's contract administration system. Bechtel felt strongly this should never have resulted in a claim since U.S./Cobb had sufficient entitlement to justify further negotiations.

Prior to the mini-trial, Alpha completed its report and in it concluded that Bechtel owed the government money, that is, that the claims lacked merit. Mr. Jackson contacted Col. West to ask him if there was any reason to proceed with the mini-trial in light of Alpha's findings. Col. West assured Mr. Jackson the report did not represent the final word on the Corps' position regarding the claims and that it was still worthwhile to proceed.

In their combined "position paper," Bechtel requested a total of \$6.5 million for all outstanding claims; Marathon sought additional payment of \$3.5 million to resolve its claims; and U.S./Cobb and the other subcontractors filed for the remaining amounts. The Alpha report concluded that the contractors owed the government money because Bechtel had been overpaid for work change orders. However, prior to the mini-trial the Corps found entitlement in two of the Bechtel claims, though disagreement remained over quantum. The Corps also found entitlement in some of Cobb's claims, but maintained strongly divergent views over pricing. In the case of Marathon, the Corps stood by its assessment that the claim lacked any merit.

DECISION TO USE ADR

RAISING THE OPTION OF ADR

At a time when the Corps and Bechtel were deep within the legal maze, filing motion after motion, frustrated by an overloaded, backlogged Board of Contract Appeals, Col. Steven West, District Engineer/Contracting Officer, reviewed the final contracting officer's decision that was about to be issued for a Bechtel claim and decided an ADR procedure was the best way to possibly dispose of all the claims Bechtel had submitted on the CSOC project. West determined that the Bechtel claims had some merit, but felt they were significantly overstated. He believed his final decision would likely be appealed, and so in an effort to save time and legal expense, deemed it worthwhile to invite the contractor to participate in settlement discussions. It was clear to West that litigation was not the most efficient way to handle the claims.

Col. West called Mr. Robert Monroe, a Bechtel officer, and suggested the use of ADR. Mr. Monroe decided it was worthwhile to pursue the prospect of ADR and contacted Mr. Jackson, who called Col. West to express interest in discussing the claims. After their conversation, Mr. Jackson called an outside Bechtel attorney, Mr. Jon Anderson, to obtain more information about mini-trials. Mr. Anderson contacted the Corps to request a copy of their ADR circular.³ Jackson and Anderson found the more they examined and researched the idea, the more they liked it.

Col. West and Gary Henningsen, Corps district counsel, contacted Bechtel to arrange a meeting to discuss the details of an ADR procedure. The four agreed to meet at the Denver Stapleton Airport.

PRE-ADR MEETING

Col. Steven West, Robert Jackson, Gary Henningsen, and Jon Anderson met at the Denver Stapleton Airport with the stated objective of discussing the details of the mini-trial. However, all in attendance agreed that the primary purpose of the meeting was to give the potential decision-makers an opportunity to assess each other in terms of a willingness to enter into a process that would succeed only if both sides were willing to negotiate seriously. Both sides knew that engaging in such an experiment had the potential to deliver impressive gains, but also presented a risk.

At the meeting, the decision-makers were able to assure each other of their authority to render a decision "without phone calls," and that neither was immovable regarding his side's position. Both men felt they would be able "to look each other in the eye and negotiate in good faith."

³ Engineer circular 27-1-3 contains guidelines for the use of mini-trials with respect to procedural issues and case selection.

A major issue the four discussed concerned the role of the subcontractors at the mini-trial. The Corps expected Bechtel, as prime contractor, to represent the subcontractors. This is how all other Corps mini-trials had handled subcontractor claims. Bechtel wanted the subcontractors to be full participants, i.e., members of the decision-makers panel. The Corps strongly objected on the grounds that subcontractors should not be given equal status with the prime contractor. Bechtel conceded, and a compromise was reached whereby the mini-trial schedule would be structured to allow the main subcontractors to present their own cases to the panel.

Bechtel's second demand was that the Corps agree that negotiations would center around quantum, that is, the monetary figure of the settlement, and not on the question of entitlement. In other words, Bechtel wanted an assurance that it would receive additional compensation, that there was no possibility that West would refuse entitlement on all the claims. Col. West and Gary Henningsen were able to give these assurances since they had found partial entitlement in at least two claims, though they were still awaiting the results of the Alpha investigation.

In preparation for the meeting, Henningsen prepared a standard mini-trial agreement based on the Corps prototype. They amended the agreement with regard to schedules for limited discovery, time frame, and length of presentations. Following the meeting, the attorneys were charged with working out the details of the mini-trial based on the days' discussions and formalizing an agreement.

PROS AND CONS OF ADR: THE CORPS

The Corps recognized entitlement in one claim prior to the airport meeting and was about to recognize entitlement in a second. It was not clear how the consultant would find in the others, but in general, the Corps found validity, but some inflation of alleged costs. Since the larger claims derived from acceleration and design modification orders, in the view of the Corps Legal Construction, Contract Administration, and Engineering team working on the case, it did not seem worth the high costs in terms of time and money to litigate entitlement before the Board, if a reasonable settlement could be reached.

Secondly, West believed the mini-trial provided an arena within which to exchange factual information. Given the polarization aroused in the district by the dispute, West thought it would be beneficial to incorporate staff participation into the process of determining a reasonable position, delivering the analysis, and discussing the final settlement. West also felt the process provided a mechanism by which the Corps and Bechtel could arrive at a fair and equitable agreement.

Another general attribute of ADR is that Corps technical field staff, (those most heavily invested in the previous position taken) are not in a position to block a settlement, but the experience of the district construction/engineering staff can be applied to the analysis and attempted resolution. Those involved in the daily workings of a project sometimes take harder positions and this results in claims being tried before the Board. A settlement agreed to by superiors can be considered a lack of confidence in their field personnel work. Since ADR encourages settling, it also can increase intra-agency tension. (This can be minimized by careful staff management.)

Thus, the use of ADR is not without potential risks. If the procedure fails to result in resolution, some of the preparatory costs are lost: according to Henningsen,

approximately 10-25% of such expenses. The balance, expenses for discovery and legal research, is useful for trial preparation.

PROS AND CONS OF ADR: THE CONTRACTOR AND SUBCONTRACTORS

When Col. West originally approached Bechtel with the option of a mini-trial, the contractor had little knowledge of the procedure. However, as counsel researched the option, Bechtel discovered it could easily support the process. In the words of the Bechtel decision-maker, "the more we heard, the better it sounded." In his eyes, a major advantage of ADR was that he would finally come face-to-face with a Corps decision-maker. Throughout the life of the project, Bechtel was frustrated it even had to file many of the claims. Bechtel believed many of the problems could have easily been resolved had it been able to meet with someone in authority. (Notwithstanding significant negotiations with authorized representatives of the Contracting Officer.) Thus, the chance to talk with a Corps decision-maker was a great opportunity, especially given the likely expenses associated with protracted litigation. Bechtel believed that negotiations, facilitated by the right neutral, would prove successful.

At the time the ADR option was raised, the contractor was engaged in legal sparring with the Corps. There was no way to determine when the claims would be heard. Even after trial, Bechtel would have to wait years for a decision on entitlement and only then negotiate quantum. It was impossible to tell when the contractor and its subcontractors, 50% of whom went bankrupt as a result of the project, would actually get paid. They only knew it would be a very long, expensive process. Since the mini-trial agreement allowed for subcontractor participation, Bechtel saw the additional advantage of potentially avoiding separate litigation with its subcontractors.

Finally, Bechtel determined that even if the mini-trial failed to resolve the claims, the time spent in preparation would be useful if the case went to trial. In fact, the mini-trial would guarantee access to government documents at an earlier date than if the case went before the Board.

Though ADR seemed to provide significant benefits, it was not without potential costs - a major one being that Bechtel had no guarantee that the government would settle. The meeting with Col. West allayed enough of their fears to determine the mini-trial was a rational gamble, but it still provided no concrete evidence with which to assure others in the corporation who opposed the ADR procedure.

Between the time the ADR agreement was signed and the date of the mini-trial, Alpha completed its report. It found that Bechtel owed the government money. Alpha reasoned that the government had overpaid Bechtel for the costs of modifications and impacts. When Bechtel heard of the conclusions of the report, those originally against the decision to use ADR believed they had further reason to distrust the process and the government's intent to accept entitlement. As a result of the nervousness inspired by the Alpha report, Jackson called Col. West to ensure that their Colorado discussions still held in light of the report. West assured him the report was not the final word and that it was still appropriate to proceed with the mini-trial.

